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Before The
FEDERAL COMMUNICATIONS COMMISSION

TABLE OF CONTENTS

Before The
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554

In the Matter of	)	
	)	
Implementation of Sections of the Cable Television Consumer Protection and Competition Act of 1992	)	MM Docket 92-266
	)	
Rate Regulation	)	

JOINT REPLY COMMENTS OF BELL ATLANTIC,[1] GTE,[2] AND THE NYNEX TELEPHONE COMPANIES[3] IN RESPONSE TO FURTHER NOTICE OF PROPOSED RULEMAKING

The cable industry continues to resist meaningful rate regulation. Its response to the Commission's proposed exclusion of low penetration systems reveals both an underlying hostility to the 1992 legislation and a fundamental misconception of the purpose and function of a competitive benchmark. If the industry has its way in this proceeding, monopoly cable operators will remain free to collect rates significantly above competitive levels and to reap the unwarranted financial windfall that attends the exercise of

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[1] The Bell Atlantic telephone companies ("Bell Atlantic") are The Bell Telephone Company of Pennsylvania, the four Chesapeake and Potomac telephone companies, The Diamond State Telephone Company, and New Jersey Bell Telephone Company.

[2] GTE is the GTE Service Corporation on behalf of the GTE Domestic Telephone Operating Companies and GTE Laboratories Incorporated.

[3] The NYNEX Telephone Companies include New England Telephone and Telegraph Company and New York Telephone Company.

market power. That result would nullify the core objectives of the 1992 Act.

In their opposition to the Commission's proposal, the cable operators advance four lines of attack. They argue (1) that the statute expressly prohibits the exclusion of low penetration systems; (2) that competitive systems are not representative of cable systems nationally; (3) that the rates of competitive systems and municipal systems are below true market levels; and (4) that establishing a benchmark at a truly competitive rate level would wreak havoc on the financial well-being of cable operators.

None of these arguments has merit. Indeed, only the first goes to whether low penetration systems should be excluded. The others belong more appropriately in a petition for reconsideration -- they are really collateral attacks on the Commission's decision to use a competitive benchmark as the initial standard for regulating cable rates.

1. Excluding Low Penetration Systems from the Competitive Benchmark Implements Congressional Policy and Comports with the Statutory Text

Cable's most prominent argument, echoed in nearly identical terms by every cable participant, is that the Act expressly requires the Commission to include low penetration

systems in calculating a competitive benchmark.[4] The thesis is that the statute defines "effective competition" to include low penetration systems and that eliminating such systems from the competitive benchmark would constitute an impermissible rewriting of the definition.

The argument both misreads the statute and misapprehends the Commission's proposal. Although Congress exempted low penetration systems from rate regulation, it did not require the Commission to include the rates of such systems in a competitive benchmark. On the contrary, Congress found that cable operators with no multichannel video competition (a class that includes low penetration systems) exercise undue market power.[5] In recognition of its paramount goal to protect consumers from the exercise of such market power,[6] Congress carefully directed the Commission

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[4] E.g., Comments of the National Cable Television Association (NCTA) at 1-2, 5-9; Comments of Tele-Communications, Inc. (TCI) at 4-7; Comments of Time Warner Entertainment Company, L.P. (TWE) at 4-6; Comments of Cablevision Industries Corporation et al. (Joint Parties) at 2-9; Comments of Continental Cablevision, Inc. (Continental) at 2-5; Comments of Arizona Cable Television Association et al. (Arizona Cable) at 3-5; Comments of Viacom International Inc. (Viacom) at 2-10; Comments of the Coalition of Small System Operators (Coalition) at 4-5; Comments of the Community Antenna Television Association (CATA) at 2-5.

[5] Cable Television Consumer Protection and Competition Act of 1992, Pub. L. No. 102-385, § 2(a)(2), 106 Stat. 1460 (1992) ("1992 Cable Act").

[6] Id. § 2(b)(5).

only to "take into account" -- not necessarily to rely upon -- the rates of exempt systems.[7]

As we demonstrated in our opening comments,[8] "take into account" means just what the words say -- the Commission must consider the data and evaluate it critically. The phrase calls for an exercise of sound judgment, not a mere mathematical computation. The courts have reached precisely that conclusion in construing the same phrase in other statutes.[9] The Commission properly "takes into account" the rates of all systems subject to "effective competition" (as the statute defines that term) if it concludes that a subset of those systems faces no multichannel video competition, charges rates that reflect the exercise of market power, and must therefore be excluded from the benchmark in order to achieve the overarching statutory objectives of extinguishing the effects of market power and establishing reasonable cable rates.

The authorities on which the cable operators rely do not support their argument. Unlike the situation in those cases, the Commission here does not assert "discretion to

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[7] Id. § 3(a), to be codified at 47 U.S.C. § 543(b)(2)(C)(i). See also 47 U.S.C. § 543(c)(2)(B) (in establishing the standards for unreasonable cable programming rates, the Commission "shall consider, among other factors" the rates of cable systems subject to effective competition).

[8] Joint Comments of Bell Atlantic et al. at 11-13.

[9] E.g., Small Refiner Lead Phase-Down Task Force v. EPA, 705 F.2d 506, 516 (D.C. Cir. 1983); BASF Wyandotte Corp. v. Costle, 598 F.2d 637, 662-63 (1st Cir. 1979), cert. denied, 444 U.S. 1096 (1980); Weyerhaeuser Co. v. Costle, 590 F.2d 1011, 1045 (D.C. Cir. 1978).

adopt . . . a definition of a particular term that is at odds with a definition of that very term contained in the Act itself."[10] Rather, the Commission has applied the statutory definition scrupulously by collecting and carefully evaluating the rates of each category of cable system that fits the

television operators do not have undue market power."[12] Cable's own authorities forbid such tampering with the statutory language.

2. The Sample of Competitive Systems Is Sufficiently Representative to Yield a Reliable Benchmark

Even after excluding low penetration systems, the Commission's survey contains data from 62 cable systems facing multichannel video competition.[13] Cable operators argue that the sample is too small and insufficiently representative of cable systems throughout the nation to provide a sound benchmark.[14] They also assert that the Commission's analysis of the data is fraught with statistical and econometric errors.[15]

These arguments are irrelevant to the subject of this further rulemaking. Although they are broad attacks on the Commission's methodology, they do not even arguably support cable's claim that low penetration systems should be included in the competitive benchmark.

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[12] 1992 Cable Act § 2(a)(2) and (b)(5).

[13] These include 46 systems identified by Commission as Type B and 16 identified as Type C.

[14] E.g., TCI at 2-3 and accompanying Besen & Woodbury Statement at 32; TWE at 13 and accompanying Kelley Statement at 2; Coalition at 2-3 and accompanying Shew Declaration at 7-10.

[15] TCI argues, for example, that the Commission's equation is "misspecified" because it purportedly assumes, "evidence to the contrary notwithstanding," that all differences in rates between competitive and non-competitive systems are caused by "the presence or absence of competition." TCI at 3. See also TWE at 14 and accompanying NERA Statement at 6-7.

In any event, the criticisms are baseless. The 62 competitive systems constitute virtually the entire universe of competitive situations and are the only source from which to derive a reliable benchmark. These systems are of varying

average price per channel for competitive systems was 28 percent lower than for monopoly systems.[18]

The results of the Commission's analysis in this proceeding correspond closely to the findings in other studies

3. Systems Facing Competition Do Not Charge Artificially Low Rates

Recycling an argument advanced earlier in this proceeding, the cable companies again assert that the rates of competitive systems are artificially low and cannot be relied upon in determining a competitive benchmark. According to the cable companies, competitive rates are the product of short-term price wars or even predatory pricing practices such as "greenmail."[20]

This argument bears not at all on whether low penetration systems should be included in the competitive benchmark. Rather, it amounts to a direct challenge to the use of any competitive benchmark. The Commission has already rejected this argument on the merits and should do so again.[21]

Vigorous price competition is a desirable characteristic of competitive markets. There is no more reason to assume that the rates of systems in the competitive sample are a below-market product of price wars than that they are an above-market spike in an otherwise competitive environment. By using a per-channel average rate for its

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[20] NCTA at 2, 11; TWE at 7 and accompanying Kelley Statement at 5; Coalition at 4 and accompanying Shew Declaration at 10; Joint Parties at 10.

[21] The Commission noted but rejected the contention that "rates charged by systems subject to effective competition would be skewed since short-term price wars in overbuild situations have created artificially low rates." Order ¶ 200.

benchmark, moreover, the Commission will effectively eliminate both the high and low outliers.

As for predatory pricing, the cable companies have offered nothing more than unsubstantiated allegations. They have submitted no evidence that the rates of systems facing multichannel competition are the result of predatory conduct instead of robust competition.[22] Data from the Commission's survey belies the claim. The average age of systems subject to head-to-head competition is 13.6 years, and the average age of municipal overbuilds is 10 years. (Those figures compare with an average of 10.6 years for monopoly systems.) Because below-cost pricing cannot be sustained over extended periods, it is highly unlikely that the rates of systems with those levels of maturity have been significantly affected by price wars or greenmailing. In sum, there is simply no basis for concluding that price levels in competitive localities are not the appropriate foundation for constructing a competitive benchmark.

Nor is there any support for the assertion that the rates of municipal cable systems are below competitive levels. Far from subsidizing cable service out of tax revenues,

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[22] To the extent that there have been accusations of predatory pricing in some competitive markets, they have been levelled at incumbent operators seeking to thwart competitive entry, not at fledgling systems undercutting established participants. See, e.g., Robichaux, Cable Firms Say They Welcome Competition But Behave Otherwise, Wall Street Journal at A1 (Sept. 24, 1992) ("entrenched cable operators have sought to lock out or cripple would-be competitors" by engaging in "disabling price wars"). Certainly, NCTA has not stepped forward to identify any of its members that are charging predatory rates.

municipal systems are at least as likely (given the fiscal strains under which most local governments operate) to supplement their tax revenues by charging the most profitable cable rates that a competitive market will bear. In the absence of persuasive evidence to the contrary -- and the cable companies have offered none -- the Commission must conclude that municipal overbuilds provide a reliable indication of competitive market rates.

4. The Commission's Plan Provides a Sufficient Safety Valve to Prevent Competitive Rate Rollbacks From Causing Undue Financial Harm

Several commenters suggest that low penetration systems should be included in the benchmark because the rate rollbacks that would result if such systems were excluded would inflict grave financial injury upon many monopoly cable operators.[23] The argument is untenable.

First, existing competitive systems -- those whose rates would underlie a properly constructed benchmark -- are themselves financially healthy. There is no reason why efficient systems currently operating in a non-competitive environment could not remain profitable if their rates were confined to similar competitive levels.

Second, constructing the benchmark is the beginning, not the end, of the process. Cable operators will be free to demonstrate, in light of their particular costs, that the benchmark does not provide them an adequate rate of return.

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[23] E.g., Joint Parties at 12-14; Arizona Cable at 10-14; Colony at 10-15; CATA at 6-7; TWE at 2-3.

If an operator makes that showing, its rates will be set accordingly, and the benchmark will not adversely affect its financial soundness.

Some cable commenters suggest that the Commission and local regulators will be inundated with requests for cost-

current rate level."[26] Few cable operators will be willing to "assume[] the risk"[27] of such a downward adjustment unless special circumstances genuinely prevent them from earning an adequate rate of return on the basis of competitive rates.

CONCLUSION

To fulfill its statutory mission of ensuring that cable rates are reasonable, the Commission must exclude the rates of low penetration systems in calculating the competitive rate differential and constructing a competitive benchmark.

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[26] Order ¶ 272.

[27] Id.

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July 2, 1993

CERTIFICATE OF SERVICE

I hereby certify that a copy of the foregoing "Joint Reply Comments of Bell Atlantic, GTE and the NYNEX Telephone Companies in Response to Further Notice of Proposed Rulemaking" was served this 2nd day of July, 1993, by delivery thereof by first class mail, postage prepaid, to the parties on the attached list.

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